

Docket: : A.21-01-003  
Exhibit Number : Cal Adv - \_\_\_\_  
Commissioner : Martha Guzman Aceves  
Administrative Law Judge : Daphne Lee  
Public Advocates Office  
Witness : Prashanta Adhikari



PUBLIC ADVOCATES OFFICE



## **REPORT AND RECOMMENDATIONS ON TAXES AND RATE BASE**

**Application 21-01-003**

**San Francisco, California**

**May 25, 2021**

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## **MEMORANDUM**

1           The Public Advocates Office at the California Public Utilities Commission (Cal  
2   Advocates) examined requests and data presented by San Jose Water Company (SJWC)  
3   in Application (A.) 21-01-003 (Application) to provide the California Public Utilities  
4   Commission (Commission) with recommendations that represent the interests of SJWC's  
5   customers for safe and reliable service at the lowest cost. This Report is prepared by  
6   Prashanta Adhikari. Ting-Pong Yuen is Cal Advocates' project lead for this proceeding.  
7   Mukunda Dawadi is the oversight Program & Project Supervisor, and Angela Wuerth is  
8   the legal counsel.

9           Although every effort was made to comprehensively review, analyze, and provide  
10   the Commission with recommendations on each ratemaking and policy aspect of the  
11   requests presented in the Application, the absence from Cal Advocates' testimony of any  
12   particular issue does not constitute its endorsement or acceptance of the underlying  
13   request, or the methodology or policy position supporting the request.

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## **EXECUTIVE SUMMARY**

### **I. Introduction**

This Report presents Cal Advocates' analysis and recommendation of SJWC's income taxes, taxes other than income, and rate base for Test Year (TY) 2022 and TY 2023.

### **II. Summary of Recommendations**

#### **A. Chapter 1: Income Taxes**

To calculate TY 2022 Federal Income Tax (FIT) expense amount, the Commission should apply the 2021 State Income Tax or California Corporate Franchise Tax (CCFT) amount of \$4,603,000, the amount the Commission adopted in approving SJWC Advice Letter 556 on December 17<sup>th</sup>, 2020. SJWC recommends deducting \$3,129,200 CCFT from the taxable amount to calculate the FIT amount. Cal Advocates' recommendation results in a reduction of \$309,498<sup>1</sup> in TY 2022 FIT.

#### **B. Chapter 2: Taxes Other than Income**

1. The Commission should deny SJWC's request to escalate fixed Business License Fees of \$150,001 per year in the City of San Jose because this amount is a flat fee and does not increase during this General Rate Case (GRC) cycle. SJWC estimates Business License Fees of \$156,151 for City of San Jose Business by applying escalation factors<sup>2</sup> even though the Business License Fee in the City of San Jose will remain \$150,001 per year during this GRC period.
2. The Commission should adopt an Ad Valorem (property) tax rate of 1.2% because the rate is based on the property tax paid by SJWC in 2020. SJWC projects an Ad Valorem tax rate of 1.2100% based on an estimated property tax for 2020.

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<sup>1</sup> \$4,603,000 - \$3,129,200 = \$1,473,800 x 21% = \$309,498

<sup>2</sup> SJWC uses the inflation forecast based on HIS Global Insight US Economic Outlook August 2020 as provided by the CPUC (A.21-01-003, Exhibit F, CH-08.xlsx, WP 8-03, Cell A76).

1                   **C. Chapter 3: Rate Base**

- 2           1. The Commission should require SJWC to use at least one year of data in all  
3           expenses for lead-lag analysis to calculate working cash allowance. SJWC's use of  
4           one month of data is inadequate to calculate working cash allowance accurately.
- 5           2. The Commission should remove deferred taxes from the calculation of lead-lag for  
6           working cash allowance because deferred taxes are already included in other parts  
7           of the rate base. SJWC projects \$24,252,749 in TY 2022 and Cal Advocates  
8           recommends \$0.
- 9           3. The Commission should adopt a payroll lag of 10.58 days for lead-lag analysis to  
10          calculate working cash allowance. SJWC requested 1.32 days of payroll lag for  
11          lead-lag analysis.<sup>3</sup> SJWC's calculation of 1.32 payroll lag days does not include  
12          the employees' service period. The difference of 9.26 payroll lag days in lead-lag  
13          analysis between Cal Advocates and SJWC leads to a reduction in working cash  
14          allowance of \$835,500.
- 15          4. The Commission should adopt a state income tax lag of 57.16 days in lead-lag  
16          analysis to calculate working cash allowance because SJWC is not calculating the  
17          CCFT lag correctly. SJWC recommends -27.55 days. The difference of 84.7 lag  
18          days of income tax in lead-lag analysis between Cal Advocates and SJWC leads to  
19          a reduction in working cash allowance of \$12,413,600.
- 20          5. The Commission should authorize SJWC a working cash allowance of  
21          \$28,758,129 in TY 2022 and \$29,329,208 in 2023 as opposed to SJWC's request  
22          of \$45,152,261 in TY 2022 and \$47,169,908 in 2023. Cal Advocates'  
23          recommendation reduces working cash allowance by \$16,394,132 in TY 2022 and  
24          \$17,840,699 in 2023.

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<sup>3</sup> A.21-01-003, Exhibit F, LL Analysis, LL-01, Cell D22.



# **CHAPTER 1: INCOME TAXES**

## **I. Introduction**

This chapter presents Cal Advocates' recommendations for Income Taxes for San Jose Water Company's (SJWC) general rate case (GRC) Application (A.) 21-01-003. Income Tax expenses consist of Federal Income Tax (FIT) and California State Income Tax, also known as California Corporate Franchise Tax (CCFT). Cal Advocates' recommendations are based on analysis of SJWC's Application, testimony, workpapers, and SJWC's responses to Cal Advocates' discovery requests. Cal Advocates' Results of Operation (RO) Table 6-2 compares in detail Cal Advocates and SJWC's CCFT and FIT for TY 2022.

## **II. Summary of Recommendations**

To calculate TY 2022 Federal Income Tax (FIT) expense amount, the Commission should apply the 2021 State Income Tax or California Corporate Franchise Tax (CCFT) amount of \$4,603,000, the amount the Commission adopted in approving SJWC Advice Letter 556 on December 17th, 2020. SJWC recommends deducting \$3,129,200 CCFT from the taxable amount to calculate the FIT amount. Cal Advocates' recommendation results in a reduction of \$309,498 in TY 2022 FIT.

## **III. Discussion**

SJWC used an incorrect estimate for 2021 CCFT in calculating the company's TY 2022 FIT expense. When calculating the FIT amount, the IRS allows SJWC to deduct previous-year CCFT amount from federally taxable income in the current year. Commission Decision (D.) 89-11-058 provides guidance on how to deduct prior year

1 CCFT<sup>4</sup> which requires that the deduction be a previously adopted amount, not a new  
2 amount calculated based on estimated costs in the GRC application. The Commission  
3 reaffirmed this requirement in D.17-06-008.<sup>5</sup>

4 In the current GRC application, SJWC estimates a CCFT amount of \$3,129,200<sup>6</sup>  
5 for 2021 based on the estimated 2021 costs and uses this amount to calculate TY 2022  
6 federal income tax. An estimate of 2021 CCFT should not be used for deduction when  
7 the authorized 2021 CCFT amount is available. The Commission authorized a CCFT of  
8 \$4,603,000 when it approved SJWC Advice Letter 556 which enabled the utility to  
9 recover this amount from its customers in 2021.<sup>7</sup> SJWC's customers will pay \$4,603,000  
10 CCFT expenses in 2021 through water rates.

11 Therefore, SJWC should not use the estimated lower 2021 CCFT amount of  
12 \$3,129,200 to calculate TY 2022 federal taxable income because it is contrary to the  
13 Commission Decisions stated above, and negatively impacts SJWC's customers. In 2021,  
14 SJWC's customers are being charged a CCFT amount of \$4,603,000, the amount the  
15 Commission authorized in approving SJWC Advice Letter 556 on December 17th, 2020.  
16 By using the lower CCFT amount of \$3,129,200 to calculate the Federal Tax amount,  
17 SJWC is inflating the estimation of TY 2022 FIT by \$309,498<sup>8</sup>.

18 To calculate the FIT amount in TY 2022, SJWC should deduct the CCFT amount  
19 of \$4,603,000 paid by SJWC's customers in 2021. As SJWC's customers will fund the  
20 larger CCFT amount in 2021, they should also receive the appropriate benefit of the  
21 higher CCFT deduction in 2022. This would be consistent with federal tax law and  
22 previous Commission decisions.

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<sup>4</sup> D.89-11-058, p. 10. Conclusion of Law 1.

<sup>5</sup> D.17-06-008, Discussion Section, page 38.

<sup>6</sup> A.21-01-003, Exhibit F, CH-10A\_2021-2023, WP 10A-01, Cell G35.

<sup>7</sup> SJWC Advice Letter ADV 556, Attachment C Part II.

<sup>8</sup> \$4,603,000 - \$3,129,200 = \$1,473,800 x 21% = \$309,498

Because of the reasons stated above, the Commission should require SJWC to deduct the 2021 authorized CCFT amount of \$4,603,000 to calculate the Federal Income Tax amount in TY 2022.

## IV. Conclusion

The Commission should apply the 2021 adopted CCFT amount in calculating SJWC's TY 2022 FIT expense, as shown in Cal Advocates RO Table 6-2.

[END OF CHAPTER]

## **CHAPTER 2: TAXES OTHER THAN INCOME**

### **I. Introduction**

This chapter presents Cal Advocates' analysis and recommendations for Taxes Other Than Income for San Jose Water Company (SJWC) GRC A.21-01-003 for TY 2022. Taxes Other Than Income include Ad Valorem taxes (property taxes), Business License Fees, Franchise Taxes, and Payroll Taxes. Cal Advocates' TY 2022 recommendations for Taxes Other Than Income are primarily based on analysis of SJWC's Application, testimony, workpapers, and SJWC's responses to Cal Advocates' data requests.

### **II. Summary of Recommendations**

1. The Commission should not allow SJWC to escalate fixed Business License Fees of \$150,001 per year in the City of San Jose because this amount is a flat fee and does not increase during this General Rate Case (GRC) cycle. SJWC estimates Business License Fees of \$156,151 for City of San Jose Business by applying the escalation factors<sup>2</sup> even though the Business License Fee in the City of San Jose will remain \$150,001 per year during this GRC period.
2. The Commission should adopt an Ad Valorem tax rate of 1.20% because the rate is based on the property tax paid by SJWC in 2020. SJWC projects an Ad Valorem tax rate of 1.2100% based on an estimated property tax for 2020.

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<sup>2</sup> SJWC uses the inflation forecast based on HIS Global Insight US Economic Outlook August 2020 as provided by the CPUC (A.21-01-003, Exhibit F, CH-08.xlsx, WP 8-03, Cell A76).

### 1    **III.    Discussion**

#### 2                    **A.   Business License Fees**

3                SJWC states that it pays a flat fee of \$150,001 per year in the City of San Jose, as  
4   of 2017, and a \$12 per-hydrant fee in the City of Los Gatos.<sup>10</sup> Even though SJWC pays a  
5   fixed amount of business license fee to the City of San Jose, SJWC projects Business  
6   License Fees in TY 2022 by escalating the total estimated amounts from 2021. SJWC's  
7   estimate is incorrect because it is currently escalating total Business License Fees on a  
8   year-to-year basis. In TY 2022, the escalation factor is 1.041.<sup>11</sup> Cal Advocates opposes  
9   this methodology for calculating Business License Fees.

10              SJWC's method of escalating a fixed business license fee for TY 2022 estimation  
11   is improper because SJWC is not reflecting the flat fee amounts. Since the business  
12   license fee in the City of San Jose is a fixed amount, there is no need to authorize more.  
13   SJWC should only escalate the per-hydrant fee in the City of Los Gatos but use the flat  
14   fee in the City of San Jose for in projecting TY 2022 Business License Fees. Because  
15   SJWC is calculating Business License Fees by escalating yearly rather than showing the  
16   number of hydrants in Los Gatos, this allows for potential increases to the number of  
17   hydrants while not allowing the flat fee in the City of San Jose to be escalated.

18              Escalating the hydrant fee of \$16,041 for the City of Los Gatos and a fixed fee of  
19   \$150,001 for the City of San Jose would result in TY 2022 Business License Fees of  
20   \$163,661 rather than the \$172,252 currently projected by SJWC. The Commission should  
21   adopt total Business License Fees of \$163,661 for SJWC in TY 2022.

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<sup>10</sup> A.21-01-003, Exhibit F, CH-10, WP 10-05

<sup>11</sup> A.21-01-003, Exhibit F, CH-08, WP 8-03, Cell H70.

1                   **B. Payroll Taxes**

2                   **1. FICA Taxes**

3                   Cal Advocates does not oppose SJWC's method for calculating FICA taxes. The  
4                   Federal Government collects taxes to fund Social Security and Medicare. The current  
5                   FICA tax rate for Social Security is 6.2%, up to \$137,000 in earnings and 1.45% for  
6                   Medicare, with no maximum earning limit for paying taxes. Thus, the total tax rate is  
7                   7.65% for up to \$137,000 in earnings, with an additional 1.45% for any earnings above  
8                   that. Based on the previous five years of SJWC's FICA taxes divided by total direct  
9                   payroll, SJWC has an average FICA tax rate of 6.75%. SJWC is multiplying this rate by  
10                  the projected TY 2022 total direct expense payroll. Any differences in total FICA tax  
11                  amounts between SJWC and Cal Advocates result from different estimations of the  
12                  number of employees and salaries recommended in the Direct Testimony of Cal  
13                  Advocates witness, Mr. Ting-Pong Yuen.

14                  **2. FUI and SUI Taxes**

15                  Cal Advocates does not oppose SJWC's methodology for calculating FUI and SUI  
16                  taxes. Both California and the Federal Government collect taxes to fund Unemployment  
17                  from the first \$7,000 of each employee's salary. The state rate is 2.4%, and the federal  
18                  rate is 0.6%. SJWC is currently projecting 406 employees with authorized positions in  
19                  TY 2022. With some turnover and part-time/temporary employees, SJWC projects total  
20                  FUI taxes of \$12,700 and SUI taxes of \$52,700.<sup>12</sup>

21                  Any differences in total FUI and SUI tax amounts between SJWC and Cal  
22                  Advocates are the result of different estimations of the number of employees and salaries  
23                  recommended in the Direct Testimony of Cal Advocates witness, Mr. Ting-Pong Yuen.

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<sup>12</sup> A.21-01-003, Exhibit F, CH-10, WP 10-06.

1                   **C. Ad Valorem Taxes**

2           The Commission should approve an Ad Valorem tax rate of 1.2% for TY 2022  
3 because the tax rate is based on more recent SJWC data. SJWC miscalculates the Ad  
4 Valorem tax rate of 1.21%. SJWC should use the five-year average rate (2016-2020) of  
5 1.2% to calculate the Ad Valorem taxes amounts for TY 2022. In the current GRC  
6 application, SJWC provides different numbers for the estimate of 2020 Ad Valorem  
7 Taxes. SJWC's GRC Application Chapter 10 of Exhibit F on taxes other than income  
8 shows two different numbers for Ad Valorem Taxes. The two projections for 2020 Ad  
9 Valorem taxes are \$10,498,758 and \$10,972,630.<sup>13</sup>

10           To calculate the Ad Valorem tax rate, SJWC uses hardcoded<sup>14</sup> numbers for both  
11 Ad Valorem tax expense and market value of utility property.<sup>15</sup> To find how SJWC came  
12 up with those numbers, Cal Advocates calculated the averages of the past five years of  
13 taxes paid and utility property value, including the different values of property taxes  
14 mentioned above. This showed that SJWC was using the higher number, \$10,972,630, to  
15 calculate the hardcoded number.

16           When asked about this discrepancy in a data request, SJWC explains that  
17 “[a]mounts cited in WP 10-2 and WP 10-3 were estimates of year end. Final year end  
18 amounts for 2020 will be updated in the 45-day update of Exhibit F.”<sup>16</sup>

19           While SJWC provided a new number for TY 2020 Ad Valorem taxes in its  
20 workpapers from the 45 day-update totaling \$10,639,249,<sup>17</sup> SJWC still used the original  
21 projection of the Ad Valorem tax rate, based on the numbers on the application, to project

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<sup>13</sup> A.21-01-003, Exhibit F, CH-10, WP 10-02, Cell K14 and WP 10-03, Cell G17.

<sup>14</sup> Hardcoded numbers are numbers simply written in Excel, without any formula or references to other cells.

<sup>15</sup> A.21-01-003, Exhibit F, CH-10, WP 10-04

<sup>16</sup> Response to DR PA-03, Question 6A.

<sup>17</sup> 45 Day Update to A.21-01-003, Exhibit F, CH 10, WP 10-02, Cell K14.

1 TY 2022 property taxes.<sup>18</sup> SJWC's 45-day update shows Ad Valorem Taxes from 2016-  
2 2020 averaging \$9,285,718.<sup>19</sup> When the five-year average of Ad Valorem taxes is  
3 divided by the average market value of utility property, \$771,200,000<sup>20</sup>, an average five-  
4 year Ad Valorem tax rate of 1.2% is found. This is lower than the 1.2100% Ad Valorem  
5 tax rate proposed by SJWC in the application. The Commission should approve an Ad  
6 Valorem tax rate of 1.2% for TY 2022 because the tax rate is based on more recent SJWC  
7 data.

8 The differences in the estimation of Utility Plant in Service between Cal  
9 Advocates and SJWC may lead to further changes in the total Ad Valorem tax amount.  
10 The Commission should adopt the projection of property taxes recommended in Table 5-  
11 1 of Cal Advocates' RO Model.

#### 12 **D. Franchise Taxes**

13 Cal Advocates does not oppose SJWC's projection of the Franchise tax rate for  
14 TY 2022. SJWC uses the 2020 Franchise tax rate of 0.2409% to estimate the Franchise  
15 tax amount for 2022.<sup>21</sup> Any differences between SJWC requested and Cal Advocates'  
16 recommended Franchise tax amounts result from the differences between SJWC's and  
17 Cal Advocates' projected revenue for TY 2022.

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<sup>18</sup> 45 Day Update to A.21-01-003, Exhibit F, CH 10, WP 10-04, Cell D42 and CH 10, WP 10-04, Cell D42.

<sup>19</sup> Average of 45 Day Update to A.21-01-003, Exhibit F, CH 10, WP 10-03, Cells C17 to G17.

<sup>20</sup> Average of 45 Day Update to A.21-01-003, Exhibit F, CH 10, WP 10-03, Cells C15 to G15.

<sup>21</sup> Update to A.21-01-003, Exhibit F, CH-10, WP 10-05.



#### 1 IV. Conclusion

2           The Commission should adopt Cal Advocates’ estimates of Business License  
3 Fees, Payroll Taxes, Ad Valorem taxes, and Franchise Taxes for TY 2022, as shown in  
4 Cal Advocates’ RO Table 5-1.

5 [END OF CHAPTER]

## **CHAPTER 3: RATE BASE**

### **I. Introduction**

This chapter presents Cal Advocates' analysis and recommendations regarding SJWC's proposed Rate Base for TY 2022 and 2023, including working cash allowance, deferred taxes, and adjustments to the utility plant. SJWC's Rate Base calculation for 2024 will not be evaluated herein, as the Rate Base for 2024 is prescribed by the current Rate Case Plan (RCP).<sup>22</sup> SJWC's Results of Operation model also reflects the formulaic calculation for rate base as guided by the Rate Case Plan. Cal Advocates' TY 2022 and 2023 recommendations for Rate Base are primarily based on its review and analysis of SJWC's Application, testimony, workpapers, and analysis of SJWC's responses to the Cal Advocates' data requests.

### **II. Summary of Recommendations**

1. The Commission should require SJWC to use at least one year of data in all expenses for lead-lag analysis to calculate working cash allowance. SJWC's use of one month of data is inadequate to calculate working cash allowance accurately.
2. The Commission should remove deferred taxes from the calculation of lead-lag for working cash allowance because deferred taxes are already included in other parts of the rate base. SJWC projects \$24,252,749 in TY 2022 and Cal Advocates recommends \$0.
3. The Commission should adopt a payroll lag of 10.58 days for lead-lag analysis to calculate working cash allowance. SJWC requested 1.32 days of payroll lag for lead-lag analysis.<sup>23</sup> SJWC's calculation of 1.32 payroll lag days does not include the

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<sup>22</sup> The Rate Case Plan states that all rate base items are subject to two test years and an attrition year, consistent with D.04-06-018 (Page A-19). Per footnote 6 on p. 15 of D.04-06-018, "the attrition allowance methodology provides for rate base additions in year 3 by adding the difference between test year 1 and test year 2 rate bases to the test year 2 rate base. Depreciation expense is handled in the same way."

<sup>23</sup> A.21-01-003, Exhibit F, LL Analysis, LL-01, Cell D22.

employees' service period. The difference of 9.26 payroll lag days in lead-lag analysis between Cal Advocates and SJWC leads to a reduction in working cash allowance of \$835,500.

4. The Commission should adopt a state income tax lag of 57.16 days in lead-lag analysis to calculate working cash allowance because SJWC is not calculating the CCFT lag correctly. SJWC recommends -27.55 days. The difference of 84.7 lag days of income tax in lead-lag analysis between Cal Advocates and SJWC leads to a reduction in working cash allowance of \$12,413,600.
5. The Commission should authorize a working cash allowance of \$28,758,129 in TY 2022 and \$29,329,208 in 2023 as opposed to SJWC's request of \$45,152,261 in TY 2022 and \$47,169,908 in 2023. Cal Advocates' recommendation reduces working cash allowance by \$16,394,132 in TY 2022 and \$17,840,699 in 2023.

### **III. Discussion**

#### **A. Allowance of Working Cash**

Working cash allowance is the money SJWC is allowed to recover from SJWC's customers so investors can earn a rate of return on day-to-day cash needs, arising from the lag between the payment of expenses and collection of revenues.<sup>24</sup> A lead-lag analysis is a study of how much working cash funding is necessary to operate the utility on a day-to-day basis. The two primary components of a lead-lag analysis are revenue lag, the time between customers receiving and paying their bills, and expense lag, the time between a utility facing an expense and when the expense is paid. An example of an expense lag is the payroll lag, which measures the time between employees providing their labor and the utility needing to pay them. This is typically done by calculating the time between the midpoint of a pay period, a service period, and the date employees are paid.

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<sup>24</sup> Ghadessi, M. & Zafar, M. (2017). Utility General Rate Case – A Manual for Regulatory Analysts. *California Public Utilities Commission Policy & Planning Division*, P. 27.

## **1. Lead Lag Reporting Requirement**

Some components of SJWC's working cash lead-lag analysis are inadequate, leading to an inaccurate and higher working cash allowance amount. For example, SJWC calculates expense lag days for purchased power by using only payment data from August 13, 2019 to September 12, 2019.<sup>25</sup> Because power is a monthly expense, one month out of a year is not enough to comprehensively analyze the average time it takes to pay off the expense fully, as one month out of 12 is 8.33% of the year. Some costs, such as income taxes, are quarterly payments, but every month of the year is still reported to calculate the income tax expense lag.<sup>26</sup> While Cal Advocates accepts the current projection of purchased power lag days, in future GRC applications, the Commission should require SJWC to calculate lead-lag days based on at least one year of payments for all its expense categories.

## **2. Expense Lag**

### **a. Deferred Tax Lag**

SJWC's working cash calculation improperly includes deferred taxes in the calculation of expense lag. Commission Standard Practice U-16-W on Determination of Working Cash Allowance states:

...the Commission, in fixing rates, has permitted normalization of the income tax expense, thereby offsetting the reduction in the tax, but has deducted from the rate base the average accumulated deferred taxes due to accelerated amortization. Therefore, for those utilities where rates have been set on this 1-17 procedure, the lag days for the offsetting amount due to accelerated amortization should be zero.<sup>27</sup>

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<sup>25</sup> A.21-01-003, Exhibit F, LL Analysis, LL-103.

<sup>26</sup> A.21-01-003, Exhibit F, LL Analysis, LL-135.

<sup>27</sup> Standard Practice U-16-W P. 1-16 – 1-17.

Despite this Standard Practice, SJWC includes a deferred tax amount of \$24,252,749 in its calculation of expense lag in the GRC application.<sup>28</sup> SJWC uses deferred tax amounts of \$1,358,659 for lead-lag analysis from the Accelerated Cost Recovery System (ACRS) and \$22,894,090 from the Modified Accelerated Cost Recovery System (MACRS).<sup>29</sup> ACRS and MACRS are tax rules for recovering the cost of property used to produce income through depreciation deductions.<sup>30</sup> ACRS is for property first used before 1987 and MACRS is for property first used after 1986.<sup>31</sup>

SJWC already includes ACRS and MACRS amounts as reductions to deferred federal taxes. The \$24,252,749 is multiplied by the federal tax rate of 21%, and then included as part of additions to Deferred Federal Income Tax.<sup>32</sup> Because ACRS and MACRS amounts are already included in rate base, the Commission should remove deferred taxes from the calculation of expense lag.

#### **b. Payroll Lag**

The Commission should adopt a payroll lag of 10.58 days. SJWC incorrectly calculated the payroll lag in the original application. Rather than the average date of the payroll period, as SJWC calculated the payroll lag in the last GRC, SJWC uses hardcoded dates,<sup>33</sup> often outside the payroll period, as the date of the expense. There are also some negative lag days, which would mean SJWC was paying employees before the end of the pay

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<sup>28</sup> A.21-01-003, Exhibit F, LL Analysis, LL-01, Cell C42.

<sup>29</sup> A.21-01-003, Exhibit F, CH-10A\_2021-2023, WP 10A-22 Def Tax.

<sup>30</sup> <https://support.cch.com/kb/solution.aspx/000045632>.

<sup>31</sup> <https://support.cch.com/kb/solution.aspx/000045632>.

<sup>32</sup> CH-13, WP 13-12, K29.

<sup>33</sup> 45 Day Update to A.18-01-004, LL Analysis, LL-104.

period.<sup>34</sup> In its response to DR PA003, SJWC acknowledged the error and indicated it will correct it in its 45-day update.<sup>35</sup>

SJWC uses the correct methodology in its 45-day updates, resulting in an increase from SJWC's original calculation of 1.32 lag days to a new number, 10.58 payroll expense lag days.<sup>36</sup> This calculation is based on Standard Practice U-16-W. The U-16-W states, "[f]or company labor, the number of lag days is the time from the midpoint of the pay period to the date of payment."<sup>37</sup> The increase in payroll lag influences other aspects of total expense lag as well. For example, payroll expense lag is a part of transferred administrative expense lag.<sup>38</sup> With an increase in the payroll expense lag, transferred administrative expense lag also increases from 2.34 to 7.44 days. The Commission should adopt a payroll lag of 10.58 days.

### **c. State Income Tax Lag**

The Commission should adopt a state income tax expense lag of 57.16 days to calculate the allowance for working cash for TY 2022 and 2023 and reject SJWC's use of negative 27.55 days of State Income Tax (CCFT) lag days to calculate the allowance for working cash for TY 2022 and 2023.<sup>39</sup> By proposing negative CCFT lag days, SJWC suggests that it will pay state income taxes nearly a month early in TY 2022 and 2024. Hence, SJWC's proposal of negative CCFT lag days is not reasonable. A review of SJWC's previous rate cases shows that SJWC has not had a negative CCFT lag day for at least fifteen years. The lowest CCFT lag over the past fifteen years was 41.62 days in 2012.<sup>40</sup> In the

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<sup>34</sup> A.21-01-003, Exhibit F, LL Analysis, LL-104.

<sup>35</sup> Response to DR PA-03, Question 2.

<sup>36</sup> 45 Day Update to A.21-01-003, Exhibit F, LL Analysis, LL-104.

<sup>37</sup> Standard Practice U-16-W, P. 1-15.

<sup>38</sup> A.21-01-003, Exhibit F, LL Analysis, LL-127.

<sup>39</sup> 45-Day Update to A.21-01-003, Exhibit F, LL Analysis, LL-136, Cell I38.

<sup>40</sup> A.12-01-003, Exhibit F, WTRLAG, WTRLAG-2010, Cell I368.

previous GRC, the Commission adopted CCFT lag days of 57.33 for 2018.<sup>41</sup> There have not been significant changes to state tax laws since 2018 that would necessitate this change.<sup>42</sup>

Additionally, according to the state franchise tax board's quarterly payment schedule, SJWC's calculation of the CCFT expense lag days is incorrect. The franchise tax board has provided a timetable for quarterly tax payments. As per the schedule, 30% of all state taxes are due on or before April 15<sup>th</sup>, 40% due on or before June 15<sup>th</sup>, 0% on or before September 15<sup>th</sup>, and 30% on or before January 18<sup>th</sup> of the following year.<sup>43</sup> To calculate the CCFT expense lag, SJWC is currently showing a payment on September 15<sup>th</sup>, when a payment is not due, and not showing any payments for the last quarter when there is a payment due.<sup>44</sup>

Therefore, the CCFT lag proposed by SJWC is not reasonable. To estimate a reasonable CCFT lag day for this GRC, the Commission should use the average CCFT lag days of the last three GRCs (2012, 2015, and 2018). The CCFT lag days in 2012 and 2018 were 41.62 and 57.33, respectively. The CCFT lag for the 2015 GRC was 72.54 days.<sup>45</sup> The average of these three CCFT lag days is 57.16. Hence, the Commission should adopt a state income tax expense lag of 57.16 days.

### **3. Allowance for Working Cash Adjustment and Allowance Amount**

Based on the recommended changes to various aspects of the expense lag mentioned above, the Commission should adopt working cash allowance of \$26,901,840 in TY 2022 and \$27,407,908 in 2023. In the 45-day update, SJWC is proposing \$45,152,261.90 and \$47,169,908.29 in 2022 and 2023, respectively for working cash allowance.<sup>46</sup> The 45-day

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<sup>41</sup> 45-Day Update to A.18-01-004, Exhibit F, LL Analysis, LL-136, Cell I38.

<sup>42</sup> <https://www.ftb.ca.gov/tax-pros/law/corporation-tax-law-changes.html>.

<sup>43</sup> <https://www.ftb.ca.gov/pay/estimated-tax-payments.html>

<sup>44</sup> 45-Day Update to A.21-01-003, Exhibit F, LL Analysis, LL-136.

<sup>45</sup> 45-Day Update to A.15-01-002, Exhibit F, LL Analysis, LL-136, Cell I38.

<sup>46</sup> 45-Day Update to A.21-01-003, Exhibit F, CH. 13, WP 13-01.

update is relevant in this matter because of the change to payment expense lag SJWC updated in its response to the data request sent by Cal Advocates, DR PA-03, mentioned above.

Because working cash allowance is a formulaic calculation based on the difference between the revenue lag of 50.3 days<sup>47</sup> and the expense lag, the methodology is the same between SJWC and Cal Advocates. However, inputs differ based on the difference in calculation of lag days. Cal Advocates' recommended changes to various expense lags (i.e. CCFT expense lag) mentioned above lead to changes in the overall expense lag days, impacting the total working cash allowance amount. Cal Advocates recommends an expense lag of 30.0 days in TY 2022 and 30.4 days in 2023. After Cal Advocates' discovery, SJWC updated expense lag days with 16.2 in TY 2022 and 16.0 days in 2023 in its 45-day updates.<sup>48</sup>

Any other differences between Cal Advocates recommended and SJWC requested allowance for working cash amounts results from Cal Advocates witnesses' recommendation of expense amounts, which may change expense lag days.<sup>49</sup> The reduction of working cash allowance also leads to a reduction in rate base.

## **B. Weighted Average Utility Plant**

The Commission should adopt Cal Advocates' recommendation for weighted average utility plant, reflected in Cal Advocates' Results of Operation Table 7-1. Cal Advocates does not oppose SJWC's methodology for calculating weighted average utility plant. While Cal Advocates uses the same methodology for calculating the weighted average utility plant, Cal Advocates recommended weighted average utility plant amount is different because of adjustments made in recorded plants and proposed plants for TY 2022 and 2023, which is

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<sup>47</sup> 45-Day Update to A.15-01-002, Exhibit F, LL Analysis, LL-02, Cell D16

<sup>48</sup> 45-Day Update to A.15-01-002, Exhibit F, LL Analysis, LL-02 and LL-03. Cell D45.

<sup>49</sup> See the Direct Testimonies of Andrew Sweeney for the Operation and Maintenance Expense Amount Recommendation and the Direct Testimony of Ting-Pong Yuen for Administrative and General Expense and Payroll & Benefits Expense Recommendation.



described in Cal Advocates' plant testimonies.<sup>50</sup> SJWC proposes a weighted average utility plant of \$2,083,292,300 in TY 2022 and \$2,257,317,700 in 2023.<sup>51</sup> To Calculate weighted average plant amounts, SJWC adds weighted average additions to the beginning of year plant balance.<sup>52</sup> Weighted average plant additions are weighted net plant additions to utility plant multiplied by the five-year weighted average factor,<sup>53</sup> which divides the past five years of weighted average additions by net additions.<sup>54</sup>

### **C. Adjustment to Utility Plant**

Cal Advocates does not oppose SJWC's calculation of Adjustment to Utility Plant in TY 2022. SJWC deducts \$221,492,700 from the rate base for Adjustment to Utility Plant in TY 2022. The Adjustment to Plant comprised of Advances for Construction, Contributions in Aid of Construction, Plant Funded by Safe Drinking Water State Revolving Fund (SDWSRF) Loan, and Reserve for Amortization of Intangibles.<sup>55</sup> Because SJWC's investors do not fund these items, they are deducted from the rate base.

The four items mentioned above sum up to total Adjustment for Utility Plant of \$221,492,700.<sup>56</sup> SJWC estimates \$78,475,900 in Advances for Construction which are payments received from customers for construction projects that must be refunded. While Contributions in Aid of Construction, set at \$142,061,100, are similar, they are non-refundable funds. The SDWSRF loan amount of \$370,200 is provided by the California Water Boards to finance the cost of infrastructure projects needed for compliance with Safe

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<sup>50</sup> Direct Testimony of Daphne Goldberg, Direct Testimony of Phong Ly, Direct Testimony of Niamh Murphy, and Direct Testimony of Isaac Gendler.

<sup>51</sup> A.21-01-003, Exhibit F, CH. 13, WP 13-01.

<sup>52</sup> A.21-01-003, Exhibit F, CH. 11, WP 11-01.

<sup>53</sup> A.21-01-003, Exhibit F, CH. 11, WP 11-03.

<sup>54</sup> A.21-01-003, Exhibit F, CH. 11, WP 11-05, Cell G24.

<sup>55</sup> A.21-01-003, Exhibit F, CH-13, WP 13-01, Cell M14.

<sup>56</sup> A.21-01-003, Exhibit F, CH-13, WP 13-04.

Drinking Water Act requirements. Finally, SJWC estimates \$585,500 for the Reserve for Amortization of Intangibles, which is for expensing the cost of intangible assets over the life of the asset for accounting purposes.

#### **D. Depreciation Reserve**

Cal Advocates follows the same methodology in calculating weighted average depreciation reserve as SJWC does. Any differences between Cal Advocates' recommended and SJWC's requested weighted average depreciation reserve amounts result from the differences in plant recommendations. SJWC estimates and deducts from the rate base a weighted average depreciation reserve of \$754,546,700 for TY 2022 and \$818,729,200 for TY 2023.<sup>57</sup> Depreciation reserve is the total depreciation expense that has been recognized on fixed assets, and thus, deducted from the rate base. SJWC calculates the weighted average depreciation for TY 2022 by adding weighted average addition of depreciation expense to the beginning of the year depreciation balance.<sup>58</sup> The weighted average depreciation additions are calculated by multiplying the net change in depreciation reserve by the five-year weighted average factor of 0.5329.<sup>59</sup> The five-year weighted average factor is the past five years (2016-2020) of weighted average additions divided by net additions.<sup>60</sup>

#### **E. Deferred Tax**

Cal Advocates does not oppose SJWC's calculation of deferred tax. SJWC deducts \$135,481,670 in deferred taxes from the rate base in TY 2022.<sup>61</sup> SJWC calculates deferred tax amount by adding the balance of the investment tax credit reserve of \$864,600, to the

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<sup>57</sup> A.21-01-003, Exhibit F, CH-13, WP 13-01, Cells M31 and N31.

<sup>58</sup> A.21-01-003, Exhibit F, CH-12, WP 12-01, Cell L14.

<sup>59</sup> A.21-01-003, Exhibit F, CH-12, WP 12-01, Cell L37.

<sup>60</sup> A.21-01-003, Exhibit F, CH-12, WP 12-03, Cell G22.

<sup>61</sup> A.21-01-003, Exhibit F, CH-13, WP 13-01, Cell M20.

average of the beginning and end-of-year deferred federal income tax balances of \$134,617,070.<sup>62</sup>

#### **F. Rate Base, Taxed Contributions**

Cal Advocates does not oppose SJWC's calculation of rate base, taxed contributions. SJWC estimates \$11,673,589 in TY 2022 for taxed contribution additions to rate base.<sup>63</sup> This is based on a sum of taxable contributions from 1992 to 2022, with the rates increasing on a yearly basis.<sup>64</sup>

#### **G. Rate Base, Taxed Advances**

Cal Advocates does not oppose SJWC's calculation of rate base, taxed advances. SJWC estimates \$3,183,898 in TY 2022 for taxed advances on rate base.<sup>65</sup> SJWC calculates total taxed advances by using taxed advances amounts from 1987 to 2022.<sup>66</sup>

### **IV. Conclusion**

The Commission should adopt Cal Advocates' recommendations on rate base amounts for TYs 2022 and 2023, as presented in Cal Advocates Results of Operations Table 9-1.

[END OF CHAPTER]

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<sup>62</sup> A.21-01-003, Exhibit F, CH-13, WP 13-12, Cell K35.

<sup>63</sup> A.21-01-003, Exhibit F, CH-12, WP 13-01, Cell M22

<sup>64</sup> A.21-01-003, Exhibit F, CH-12, WP 13-07, Cell J66.

<sup>65</sup> A.21-01-003, Exhibit F, CH-12, WP 13-01, Cell M24.

<sup>66</sup> A.21-01-003, Exhibit F, CH-12, WP 13-08, Cell J66.

**ATTACHMENT 1: STATEMENT OF QUALIFICATIONS -**  
**PRASHANTA ADHIKARI**

- Q1. Please state your name, business address, and position with the California Public Utilities Commission (“Commission”).
- A1. My name is Prashanta Adhikari and my business address is 505 Van Ness Avenue, San Francisco, California 94102. I am a Public Utilities Regulatory Analyst (PURA) in the Communications Water & Policy Branch of the Public Advocates Office.
- Q2. By whom are you employed and in what capacity?
- A2. I am employed by the Commission’s Public Advocates Office as a PURA.
- Q3. Please summarize your education background and professional experience.
- A3. I have a BA in Economics from University of California, Davis (2017) and have worked as a PURA since October 2019.
- Q4. What is your responsibility in this proceeding?
- A4. My responsibility is preparing testimony on taxes and rate base and the Results of Operation Tables and report.
- Q5. Does this conclude your prepared direct testimony?
- A5. Yes.

**ATTACHMENT 2: SJWC'S RESPONSE TO CAL**  
**ADVOCATES'S DATA REQUEST PA-01**



110 W. Taylor Street  
San Jose, CA 95110-2131

February 11, 2021

Ting-Pong Yuen  
Public Advocates Office  
California Public Utilities Commission  
505 Van Ness Avenue  
San Francisco, CA 94102

**Re: Response to Data Request PA-01  
General Rate Case Application 21-01-003**

Dear Mr. Yuen:

Enclosed you will find San Jose Water Company's (SJWC) response to data request PA-01 dated February 1, 2021. The information was prepared by:

Ritu Mehta  
Director of Taxation  
408 918-7284  
[ritu.mehta@sjwater.com](mailto:ritu.mehta@sjwater.com)

Ann Lindahl  
Manager, Regulatory Affairs  
408-642-0359  
[ann.lindahl@sjwater.com](mailto:ann.lindahl@sjwater.com)

Due to the current shelter-in-place order, SJWC will only provide responses electronically. Hard copies will not be provided.

If you have any questions, please contact me.

Very truly yours,

A handwritten signature in blue ink, appearing to read 'John B. Tang', with a stylized flourish at the end.

John B. Tang, P.E.  
Vice President of Regulatory Affairs

& Government Relations

cc: Prashanta Adhikari, Public Advocates Office  
Mukunda Dawadi, Public Advocates Office  
Angela Wuerth, Public Advocates Office

## RESPONSES

1. Please provide PDF copies of San Jose Water Company's (SJWC) Federal Income Tax returns (actual complete tax return, not pro-forma) for the last three years. If SJWC's parent company, SJW Corp., files consolidated tax returns, provide the parent company's full tax returns with all schedules, and indicate which pages and portions contain information regarding SJWC.

**SJWC Response:** Please see folder DR PA-01 R.1 Federal Income Tax Returns being submitted via Kiteworks.

2. Provide PDF copies of SJWC's California Corporate Franchise Tax (CCFT) state income tax returns (actual complete tax return, not proforma) for the last three years. If SJWC's parent company, SJW Corp., files consolidated tax returns, provide parent company's full tax returns with all schedules, and indicate which pages and portions contain information regarding SJWC.

**SJWC Response:** Please see folder DR PA-01 R.2 California Income Tax Returns being submitted via Kiteworks.

3. Provide PDF copies of the Form DE-2088 that San Jose Water Company received from the State of California Employment Development Department for contribution rates for Unemployment Insurance and Employment Training Tax for 2017, 2018, 2019, 2020, and 2021.

**SJWC Response:** Please see DR PA-01 R.3 Form DE-2088 being submitted via Kiteworks.

4. Provide PDF copies of the Form 941 (Employers Quarterly Federal Tax Return) SJWC submitted to IRS in each quarter for 2017, 2018, 2019, and 2020.

**SJWC Response:** Please see folder DR PA-01 R.4 Form 941 being submitted via Kiteworks

5. On page 10-4 of the Exhibit E – RO Report, SJWC states, “.... the Company filed Form 3115 to change the method of accounting for tax purposes to comply with IRC Section 263A. The new methodology has been used in the tax workpapers.”

a. Please provide a copy of Form 3115.

**SJWC Response:** Please see DR PA-01 R.5.a Form 3115 being submitted via Kiteworks.

b. Explain the change in methodology proposed in Form 3115.

**SJWC Response:** The present methodology allocates direct and indirect costs to self-constructed property using specific identification method and excludes certain indirect costs which are required to be capitalized under I.R.C. Section 263A. The proposed methodology is to capitalize all direct and indirect cost required to be required capitalized under I.R.C Section 263A with respect to production of self-constructed assets. The additional costs will be allocated to self-constructed property using a reasonable allocation method as described in Treas. Reg. Section 1.263A-(1)(f)(4).

c. Where is this new methodology reflected in the tax workpapers?

**SJWC Response:** WP10A-01 and WP10A-22

d. How does Form 3115, mentioned on page 10-4, affect revenue requirements?

**SJWC Response:** The change as required by the I.R.C Section 263A increases tax expense as it requires capitalization of mixed service costs in the year incurred (thus they are not deductible for income tax purposes) and results in a lower deferred tax liability. As a result, it results in a higher revenue requirement. This will reverse over the tax life of the asset thus decreasing tax expense and increasing deferred tax liability in the future resulting in a lower revenue requirement. Hence, it is a timing issue.

6. In WP 10-02 cell K14 and WP 10-03 cell G17 of CH.10, there are two different ad valorem tax amounts (\$10,498,758 and \$10,972,630, respectively) for 2020. The higher amount, \$10,972,630, is used to calculate the tax rate for the last five years in cell G43 of WP 10-04. Cell L15 from WP 10-A of the RATECASE spreadsheet has the lower amount \$10,498,758 from WP 10-02.

a. What are the actual ad valorem taxes paid for 2020?

**SJWC Response:** Amounts cited in WP 10-2 and WP 10-3 were estimates of year end. Final year end amounts for 2020 will be updated in the 45 day update of Exhibit F. Please see attached excel file DR PA-01 R.6 being submitted via Kiteworks.

b. Provide the supporting documents for the total ad valorem taxes paid for 2020.

**SJWC Response:** Please see attached excel file DR PA-01 R.6 being submitted via Kiteworks.

7. In WP 10-23 RevExcessDeff, Excess Deferred Taxes are in row 14 and the reversal of excess taxes are in row 16. How is the reversal amount per year calculated? Please provide documents supporting:

a. Total Excess Deferred Taxes at the beginning of 2021.

**SJWC Response:** Please see attached excel file DR PA-01 R.7. a.b. WP 10-23 being submitted via Kiteworks.

b. The calculation of reversal of excess taxes per year.

**SJWC Response:** Please see attached excel file DR PA-01 R.7. a.b. WP 10-23 being submitted via Kiteworks.

c. The period of years over which San Jose will completely reverse excess deferred taxes.

**SJWC Response:** The Excess Deferred Taxes in row 14 and the Reversal of Excess Taxes in row 16 consist of plant related deferred taxes. Please note the deferred tax refund relating to plant differences is based on ARAM methodology. The number of years it will take to fully refund the excess deferred taxes depends on the reversal of the deferred through book depreciation on the assets. The reversal for a particular vintage and asset class starts in the year in which the book depreciation is greater than tax depreciation for that asset. It is difficult to estimate the number of years it will take for full refund of the excess deferred amount due to many layers of vintages and asset classes.



**END OF RESPONSE**

**ATTACHMENT 3: SJWC'S RESPONSE TO CAL**  
**ADVOCATES'S DATA REQUEST PA-03**



SAN JOSE WATER

110 W. Taylor Street  
San Jose, CA 95110-2131

February 16, 2021

Ting-Pong Yuen  
Public Advocates Office  
California Public Utilities Commission  
505 Van Ness Avenue  
San Francisco, CA 94102

**Re: Response to Data Request PA-03  
General Rate Case Application 21-01-003**

Dear Mr. Yuen:

Enclosed you will find San Jose Water Company's (SJWC) response to data request PA-03 dated February 5, 2021. The information was prepared by:

Ann Lindahl  
Manager, Regulatory Affairs  
408-642-0359  
[ann.lindahl@sjwater.com](mailto:ann.lindahl@sjwater.com)

Due to the current shelter-in-place order, SJWC will only provide responses electronically. Hard copies will not be provided.

If you have any questions, please contact me.

Very truly yours,

John B. Tang, P.E.  
Vice President of Regulatory Affairs  
& Government Relations

cc: Prashanta Adhikari, Public Advocates Office  
Mukunda Dawadi, Public Advocates Office  
Angela Wuerth, Public Advocates Office

## RESPONSES

Please refer to RO Model Workpaper Excel file "LL Analysis" for the following data requests.

1. In sheets LL-01, LL-02, and LL-03 of LL Analysis, Deferred Tax amounts are included as a part of expense lags. There are negative and positive amounts in Cells C42 and C43, respectively, but only the negative balance is multiplied by average lag days to calculate Total \$ Days Lag in Cell F42.
  - a. Why are both negative and positive deferred tax amounts included in column C? **SJWC Response:** The methodology has been used for the prior lead lag studies going back at least as far as 2006 for which we have access to electronic records. Additional time is needed to research the methodology and calculation.
  - b. Why is the positive balance for deferred tax amounts not included in the calculation of Total \$ Days Lag in Cell F42?  
**SJWC Response:** Additional time is needed to research the methodology and calculation.
  - c. Why is the negative balance of deferred tax amount included in the calculation of Total \$ Days Lag in Cell F42?  
**SJWC Response:** Additional time is needed to research the methodology and calculation.
  - d. Does the deferred tax amount included as part of the expense lag represent the tax SJWC paid to the IRS in advance of recovering from customers?  
**SJWC Response:** The deferred tax amount included as part of the expense lag represents the tax SJWC will pay the IRS for the year in question which is more than the tax expense being recovered from the ratepayers for that particular year.
2. Sheet LL-104 of LL Analysis calculates payroll lag days in Column I. The average lag days calculation does not include the mid-point of the work period. The calculation only accounts for the difference between the expense recorded date (Column H) and the date paid (Column I)
  - a) Why does the average lag days calculation (Column I) not include the period of work?  
**SJWC Response:** The lag should include the mid-point of the period of work. The worksheet will be corrected and provided in the Update to the Workpapers.

END OF RESPONSE